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EDUCATION
DEPARTMENT

MICHIGAN BANKING LAW

AND

DESIRABLE AMENDMENTS,

BY HON. T. C. SHERWOOD,

COMMISSIONER OF THE
STATE BANKING DEPARTMENT OF MICHIGAN.

ADDRESS

DELIVERED BEFORE THE MICHIGAN BANKERS' ASSOCIATION CONVENTION, HELD AT
DETROIT, AUGUST 9TH, 10TH AND 11TH, 1892.

Mr. President and Gentlemen of the Convention—The Program Committee, notwithstanding my protest, have assigned me this subject, "Michigan Banking Law, and Desirable Amendments," claiming that the position I occupy enables me to study the working of our State law, ascertain its weak places, and suggest remedies.

But right here is where the committee are in error, for the more I study the operation of Finance, the less I am inclined to advise as to the best methods to adopt in conducting its operations.

The more I study the State Banking Law, and witness its effect upon the banks in different localities of the State, the fewer amendments would I suggest.

The more I investigate the systems adopted by many of the banks in the State, and become acquainted with the officers of these institutions, the greater my embarrassment in standing here attempting to advise those whose opinions as to the needs of a Banking Law are of more practical value than any I may express.

To write a good article on any subject, a person must know next to nothing of the question under discussion. Then he is not hampered by prejudice, facts, or figures, and can give full play to his imagination.

I know just enough about banking to make me careful in the advice I give and the suggestions I make in regard to our Banking Law and necessary amendments. I would be a dull scholar indeed,

if in the past four years I had not learned much in studying the law, witnessing its operations in different parts of the State, its effects upon the business interests of the country, and by coming in contact with the large number of Michigan bankers, among whom are found the brightest financiers of the country.

Yet, if my experience is of value, if the knowledge of the requirements of a Banking Law obtained by actual observation will be of benefit to this Association, I most cheerfully impart it.

We are all scholars in the school of finance, and he only deceives himself and works mischief and injury to others, who thinks he has already mastered the science, and there is nothing further for him to learn.

Business principles and methods are continually undergoing changes. The financial systems of forty years ago are obsolete now, and the financier of to-day must be an attentive student if he keeps up with the procession in the race for success.

No person can in this age of the world successfully engage in a business or a profession unless he has a certain amount of confidence in his fellow men; neither can he succeed unless the public have confidence in *his* ability and faith in *his* integrity.

Law is a controlling regulation, which has for its object the building up of confidence in one another's integrity by visiting penalties upon those who violate its provisions or disregard its authority.

As there is no class of business transacted to-day which is built up and operated so exclusively on faith and confidence in the honesty and integrity of others as the banking business, it is necessary that our Banking Laws be such as will inspire confidence, which is the basis or foundation of material prosperity.

Faith in humanity is a necessary concomitant in banking. I care not how wealthy a man may be, he cannot succeed as a banker if he treats his customers as though *they* were dishonest, or is *himself* suspected by the public of being deceitful and treacherous.

Integrity begets confidence, and he who trusts no one is himself unworthy of credit or confidence.

In proof of the assertion that confidence is necessary in a banking business, I need only refer to the "wildcat" banking of Michigan, made possible by the Banking Law of 1837, which the older members of this Association so well remember.

By the systematic fraud practiced by the bankers of that day, the very system became a reproach.

The President and Cashier were looked upon as little better than

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confidence men, and the sign "Bank" upon the window or door was as significant to the average business man as was the inscription over the cave in Dante's Inferno, "Who enters here leaves hope behind."

It was not until the State bank circulation was taxed out of existence, and the establishment of the National banking system, that confidence was restored.

With National supervision and inspection our banking system was raised to a higher standard of excellence and usefulness than any system had ever attained before, and we stood before the nations of the world with the grandest and most complete banking system ever known.

In Michigan to-day the bank means something more than "Shylock's office," a place to borrow money, or barter stocks and bonds. It is now regarded as synonymous with honest dealing and mutual benefit, and is used as the depository for the surplus money of our citizens, who, as laborers, have not the time to make investments, or by business men who, for convenience, use the facilities offered by the bank for the transaction of commercial business.

Confidence once lost is not easily regained, as many corporations and individuals can testify. Therefore it is necessary that whatever Banking Law is adopted, or amendment made, it should have for its object the strengthening of public confidence in the system and faith in the wisdom of its administration.

With this end in view, the framers of Michigan's Banking Law copied largely from the National law, which for thirty years has withstood criticism and inspired confidence.

In place of the Comptroller of the Currency, as in the National Banking Law, our State law provides for the appointment of a Commissioner of the Banking Department, whose duty it is to authorize the incorporation of banks, ascertain if the required amount of capital is actually paid in, and if the business is transacted in accordance with law; call for reports from the several banks on passed days unknown to the bank officers, cause these reports to be published for the benefit of depositors and the general public, verify their correctness by a personal examination by examiners appointed by him, and exercise a general supervision over the banks incorporated under State law.

All these powers are substantially those conferred upon the Comptroller of the Currency, and have a tendency to inspire confidence in the stability and permanency of our State system.

That portion of the National law which provides for the issue of

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bank circulation, was wisely omitted by the framers of Michigan law, as Sections 32 and 62 expressly prohibit the issuing of any bill, note or certificate intended to circulate as money.

Michigan business men are satisfied with the experience they have had with State circulation, and this generation at least will refrain from adopting any amendment to our State Banking Law permitting banks to issue any note or bill intended to circulate as money. No doubt there are many bankers who would be pleased if State banks were allowed to issue circulation, as there is money in it for the banker.

In the old days of State circulation, the uncurrent money department of many of the banks was the best paying department of the institution.

The sufferers were the traveling public, the small dealers, and the laboring class, and *not* the banks which issued the currency, or the individuals whose business it was to exchange the notes which passed current in one State but not in another.

Our Banking Law differs from the National Act in that it is a dual law. It not only provides for the transaction of a commercial business, but takes in a wider range, and includes a savings department for the surplus money not needed in actual commercial transactions.

And right here is where very many of the older commercial bankers of the State antagonize our State system. They see no necessity for savings banks. They cannot understand why business should not be transacted to-day as it was thirty years ago. They paid no interest on deposits then, why should they now?

The reason that the Savings Bank exists is because of the changed condition of business affairs. Thirty years ago we were engaged in a civil war. Every dollar of money in circulation was needed to furnish army supplies, move crops, and transact the business of the country. We had no surplus money. Every dollar was in actual, active use. If it was deposited in banks, it remained there but a short time, and then only for the convenience of the depositor.

When the war was over, and business resumed its normal condition, the country found itself supplied with a great number of banks. The facilities for transacting the commercial business of the country by checks, drafts, and bills of exchange, was greater than ever before. Commercial banks were so loaded down with deposits in excess of the demands for commercial and accommodation loans, that they gave but little or no encouragement to the small depositor, who was

crowded out and compelled to keep his money in his house or loan it to his neighbor.

This arrangement did not work satisfactorily to either the neighbor borrowing or the person making the loan, as the borrower had rather negotiate a time loan at a bank where the accommodation is mutual and the transaction in a measure private, and the depositor had rather deposit his money where a division of the profits is made in the interest paid.

So you see that the Savings Bank is necessary. It is not the product of avarice or greed, but rather a public benefaction born of necessity. From a small beginning it has become a power and convenience in financial circles; and, gentlemen, the Savings Bank has come to stay. The public demands its existence. The farmer and laborer appreciate its value, and are satisfied with the Banking Law which seeks to protect their interests.

Of all the mutual benefit associations in existence to-day, the Savings Bank is the most beneficent, especially if security is taken into consideration.

When a bank pays four per cent on savings deposits, and loans its money at six per cent, the division of profits is unequally in favor of the depositor; but this is a rule of banking, and not a requirement of law, and will correct itself.

I have been inclined to the belief that in our large cities banks should not transact both a savings and commercial business; yet four years' experience has not witnessed any bad results, and it may be that the two classes can be operated as successfully under one management in cities, as I am satisfied they will continue to do in small towns and villages, in manufacturing and farming communities, where two separate institutions could not profitably exist.

It is not necessary that I take the time that could more profitably be used in discussing other subjects, in pointing out the good features of the Michigan Banking Law.

Copied as the commercial department is, from the National Banking Act, which in turn was copied from the State Banking Law of New York, it retains all the good measures of that law and adopts many others, which, with the savings department, make it peculiarly adaptable to our State and the times in which we live.

The savings department embodied in Michigan's Banking Law was modeled after the New York Savings Law, with this notable exception, the New York Savings Banks are not capitalized; they are simply mutual or charitable institutions, whose directors serve

without pay; while our Savings Banks are incorporated, with a paid up capital, and the stockholders are liable to the depositors for the amount of their stock, in addition to the said stock.

This feature guarantees the depositor a greater degree of watchfulness and care on the part of the directors in making investments, as a stockholder will be more interested in, and will give more of his time and attention to the bank in which he has invested his money, than he would if he was simply a trustee of the funds of another; and competition will secure to the depositor as high a rate of interest as is paid the depositor in the New York Savings Bank.

That Michigan's dual law is adaptable to the business of our State is evidenced by the fact that fifty-nine banks have incorporated under its provisions during the three and one-half years of its existence.

That the people are satisfied with its security is proven by the fact that on the 12th day of July last, they had on deposit in banks incorporated under Michigan's Banking Law, \$61,984,886.14, which is over \$23,000,000 more on deposit than when the law went into effect, January 7, 1889.

These facts, when fully comprehended, speak more eloquently the praise of Michigan's Banking Law than any words of commendation I may utter, and I therefore leave this part of the subject and take up that which relates to "Necessary Amendments."

What are *necessary* amendments, is a question difficult to decide, especially as we have such a variety of interests represented in different parts of the State, and where there exists such a diversity of opinion as to the best methods necessary to accomplish the same result.

As you are aware, I have during the past four years, refrained from urging or suggesting any radical change in our Banking Law, first, because of the injurious effect upon business interests which the continued agitation of financial measures produce; and secondly, the belief that a thorough trial of the law should be had before amendments are advocated or adopted.

There is not a thinking, conservative banker in the State that has not for the past twenty years had a feeling of anxiety during each session of the Legislature, fearing that some "crank," for political effect, would introduce and have adopted some measure that would disturb our finances, overturn existing relations, or create distrust in our financial institutions. Of course it would be done in the interest of the dear people, for whom they profess a sincere regard, *especially* about election time. Nearly every financial panic this country

has experienced has had its origin in the unnecessary agitation of financial matters by men who have had but little practical knowledge of the measures advocated. Like children playing with fire, so infatuated with the brightness of the illumination, they fail to realize until too late the awful effect of the conflagration caused by their indiscretion. Many a business failure can be charged directly to the United States Congress, where kindergarten financiers advocate their visionary schemes.

We all know there is just as large a volume of money in existence during a panic as there is in the most flourishing times; but unnecessary agitation of financial matters cause conservative bankers to strengthen their reserve fund, which takes just so much money from business channels. This causes a stringency in the money market. Every banker in the country, for self-protection, not only refuses to make loans, but calls in those already made. Money accumulates in bank vaults, or remains in the possession of individuals. Business becomes paralyzed, and a panic, with its train of calamities and suffering, is the result, and all brought about by an attempt to improve that which needed no radical improvement. "Rather bear those ills we have than fly to others that we know not of," is just as applicable in questions of finance as the one originally mentioned by Shakespeare.

For these reasons it is not expedient that I at this time suggest amendments to any special section of the Banking Law, but rather confine myself to such measures as will in my judgment make more effective Michigan's excellent Banking Law. The first suggestion, and the one I consider of the most importance, is the granting of more power to the Commissioner of the Banking Department.

The framers of Michigan's Banking Law were fearful that if too much authority was vested in the Commissioner, he might use it to the disadvantage of the banks under his supervision. They did not consider the safety of the depositor so much as they did their own convenience and protection. Being honest themselves, they did not realize that others might be dishonest; consequently they could not see the necessity of vesting extraordinary powers in one individual, for the controlling and restraining of that class who were inclined to be dishonest. They therefore withheld the authority necessary to make effective the very requirements deemed requisite in a general banking law; and while expecting that the Commissioner would execute the law in the interest of the creditors of banking corporations, they really left the power in the hands of the dishonest bank official,

or made its procedure so circuitous that the delinquent had ample time to accomplish his purpose.

As the banking law becomes more and more popular, a greater number of banks will incorporate under its provisions, and it would be strange indeed if among the number there are not some who will organize for the purpose of defrauding their customers. Such persons cannot be dealt with too quickly or too severely, and the Commissioner should have the authority to take immediate possession of such bank, and then, under the direction of the Court, proceed to wind up its affairs.

No Commissioner would be likely to abuse the authority vested in him, especially if he was an experienced banker, and certainly no other should be appointed to so important a position. I can speak plainly on this subject without being accused of self-interest, as my term of office is nearly ended.

I would also recommend that the surplus which the banks are required to keep be increased to an amount equal to one-third or one-half of their capital, and that the same be exempt from taxation. I am thoroughly impressed with the importance of a large surplus account, but it would be manifestly unjust to require a banking association to diminish the amount of its dividend to stockholders in order to increase the surplus account, and then have that surplus subject to taxation, especially when an increased surplus account would very materially add to the security of depositors.

Another measure would I suggest, and that is, to have more clearly defined the law governing banks transacting simply a commercial business.

There are other amendments, of less importance to the general public, which could with propriety be made to the banking law, which are well known to many of our bank officers; but it is to be sincerely hoped that no material change will be made, aside from strengthening and making more plain the law that has proved so well adapted to the wants of the public, in this great State of Michigan, of which we, as bankers, are so justly proud.

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